No. 12,965

IN THE

United States Court of Appeals

For the Ninth Circuit

HAWAIIAN FREIGHT FORWARDERS, LTD.,
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

OPENING BRIEF OF PETITIONER.

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JURISDICTIONAL STATEMENT.

The statutory provisions upon which the jurisdiction of the Tax Court of the United States and of this Court is based are Sections 272, 729, 1141 and 1142 of the *Internal Revenue Code;* 26 U.S.C. Sections 272, 729, 1141 and 1142.

Petitioner filed its tax returns for all years here involved with the Collector of Internal Revenue for the District of Hawaii at Honolulu, T. H. (Tr. 6). A notice of deficiency (Tr. 11) was mailed to petitioner at Honolulu, T. H. (Tr. 13) on February 2, 1948, and the petition therefrom (Tr. 6) was filed with the Tax Court on June 14, 1948.

The pleadings on which this action is founded are the petition of Hawaiian Freight Forwarders, Ltd. (Tr. 6), and the answer of the Commissioner of Internal Revenue (Tr. 24). The Tax Court entered its Findings of fact and Opinion on July 31, 1950 (Tr. 43) and on February 7, 1951, entered its decision (Tr. 57) that there was a deficiency in excess profits tax for the fiscal year ending November 30, 1943, of $21,424.70, and for the fiscal year ending November 30, 1944 of $7,403.23.

Petitioner on May 4, 1951, filed in the Tax Court its petition for review by this Court (Tr. 58).

CONCISE STATEMENT OF THE CASE.

The controversy involves petitioner's liability for excess profits taxes, specifically the proper method to be followed in the determination of its excess profits tax credit.

The primary question presented both here and in the Tax Court is whether petitioner may utilize the earnings experience of a predecessor partnership in determining its credit for excess profits tax purposes, or whether it is limited to the nominal credit on an invested capital basis.

Congress by Sections 740-744 of the Internal Revenue Code as amended by the Excess Profits Tax Amendments of 1941 and by the Revenue Act of 1942 enacted remedial legislation designed to avoid discrimination in excess profits taxes of certain corpora-

tions which had acquired the business and properties of predecessor corporations, partnerships, or sole proprietorships in tax free exchanges. Under these provisions ("Supplement A") petitioner would be entitled to use the earnings experience of a partnership if petitioner acquired substantially all of its properties for petitioner's stock in a tax free incorporation.

Petitioner was organized on March 13 or 14 of 1940 to acquire the business and properties of a predecessor partnership engaged in the freight forwarding business (Tr. 33-34). This partnership, Hawaiian Freight Association, had been organized in 1937 under the laws of the Territory of Hawaii with two active partners, J. C. Leffel and G. C. Ballentyne, and one inactive partner (Tr. 78), Dr. Schnack, with a total capital of approximately $17,000 (Tr. 33-35). Schnack withdrew on March 8, 1940, being paid $8,000 in cash from accumulated earnings for his nominal capital interest (10/67ths or approximately $2,534.03) and his share of the undrawn profits.

The certificate required to be filed to effect the dissolution of a partnership under Hawaiian law was filed July 2, 1940, and stated that dissolution occurred March 14, 1940 (Tr. 122-124).

Under the agreement of withdrawal (Tr. 37-40) the two remaining partners were to (and did) continue the partnership pending the formation of petitioner and the transfers to it. They were then equal partners (Tr. 33). They made cash withdrawals of a portion of the earnings and transferred the freight

forwarding business, and all of the remaining assets (having an adjusted cost basis of $30,000) to petitioner in exchange for its stock prorata to their interests (50-50) in the partnership (Tr. 33-34).

The respondent, in his notice of deficiency, determined that no gain or loss was recognized in this transfer (Tr. 16, 19, 22). He computed petitioner's credit for excess profits tax purposes on the invested capital method and on the basis of the cost of the assets to the partnership, adjusted for depreciation, and with no allowance for the value of good will transferred (valued on the petitioner's books at $90,000 but having no cost basis to the partnership). He gave no explanation for his failure to follow the "Supplement A" computation on the earnings method followed by petitioner in its returns (Tr. 132-133) and by respondent's agents in certain prior Revenue Agent's reports (Tr. 126, 127).

The evidence presented to the Court consisted of a written stipulation of facts (with two exhibits attached) (Tr. 32, 37, 40), an oral stipulation (Tr. 78-79), six documentary exhibits filed by petitioner (Tr. 78) and sixteen documentary exhibits filed by respondent (Tr. 82). Counsel made opening statements explaining and limiting the issues presented. The case was argued on typewritten briefs.

In the Tax Court the respondent contended that petitioner was not entitled to the remedial benefits of Supplement A because the withdrawal of Dr. Schnack resulted (under Hawaiian law) in the termination

of one partnership and the creation of a new one (Tr. 37, 74) and that what petitioner acquired was the assets of the new partnership. He regarded as immaterial the fact that "the properties" in any event were the same (Tr. 74).

Petitioner's contentions were that the transaction fell both within the letter and spirit of the remedial legislation and that it had acquired substantially all of the properties of what (under Hawaiian law) was a continuing partnership, and in any event, those of the partnership whose earnings experience it sought to use (Tr. 71-73, 75).

The Tax Court concluded (emphasis supplied):

(1) It was unnecessary to determine the effect of Schnack's withdrawal on the continuity of the partnership under Hawaiian law or any other law because *there was no intent that the partnership continue* (Tr. 50).

(2) *Petitioner acquired the business and most if not all of the assets* (remaining after cash distributions which were less than the earnings of the partnership) (Tr. 51).

(3) Petitioner *did not acquire substantially all of the assets of* Hawaiian Freight Association (the partnership) in exchange for its stock (Tr. 53).

(4) *Due to the variance in interests between Leffel and Ballentyne,*[1] the receipt by them of the stock of

[1]The conclusion is directly contrary to the stipulated facts.

petitioner on a 50-50 basis was not an exchange within Section 112(b)(5)[2] I.R.C. (Tr. 53).

(5) "The facts have been stipulated and as stipulated are so found"[3] (Tr. 44).

Dependent on petitioner's success on the primary question was and is a subsidiary issue; that is, whether petitioner was entitled to the retroactive application of the benefits of Sections 740-744 of the Internal Revenue Code as the same were amended by the Revenue Act of 1942. Stated differently, this question is whether petitioner's excess profits credit for its fiscal years ending in 1942 and prior years is to be computed on the basis of the earnings of the predecessor partnership.

The determination of this subsidiary issue is dependent upon whether the petitioner in effect made a valid election to have the benefits of such amendments apply to it or whether the respondent is estopped to contend otherwise.

All of petitioner's excess profits tax returns claimed excess profits credit on this basis (Tr. 132-133). It so claimed in a petition filed with the Tax Court applicable to its fiscal years ended in 1940 and 1941. Revenue Agents' reports allowed this approach (Tr. 126, 127), but the Commissioner, without explanation, disallowed it in the notice of deficiency.

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[2]This was not an issue before the Court in the view of counsel for either party, the Commissioner determined the transaction to be within Section 112(b)(5): his determination was *prima facie* correct and was accepted by petitioner.

[3]As noted above, in addition to the written stipulation, 26 exhibits were filed and an oral stipulation made.

Respondent contended below that petitioner was not entitled to compute its income on this basis even if successful on the main issue because it failed to use the magic words "Petitioner Elects" (Tr. 74, 75). Petitioner contended that it made a valid election, that the fact of its election was clear and that respondent, by his conduct and by reason of petitioner's reliance thereon, was estopped to contend otherwise (Tr. 73).

The Tax Court made no findings or determination with respect to this issue (Tr. 54).

After the entry of the Findings of Fact and Opinion the petitioner filed motions for correction and enlargement of the same and for reconsideration, and for a hearing on said motions (Tr. 4). The bases for these motions, briefly, were that the findings were inconsistent and incomplete, that the case was decided on issues neither presented nor argued, and that the Findings of Fact and Opinion were by a Division different than that to which the controversy was presented.

Hearing on these motions was had in San Francisco, November 1, 1950, before Division No. 8 (Judge Bolon B. Turner) and said motions were denied.

SPECIFICATIONS OF ERROR.

Petitioner specifies as error the following acts and omissions of the Tax Court of the United States:

1. The Court erred in assigning the controversy for determination to a Division of the Court other

than that to whom the controversy was presented, such action being without authority of law and contrary to the statutory provisions establishing the Court and providing for the manner of exercise of its functions.

2. The Court erred in having a Division other than that to whom the controversy was presented determine the same by Findings of Fact and Opinion, and decision pursuant thereto, such acts being without authority of law, contrary to the statutory provisions establishing the Court and providing for the manner of exercise of its functions.

3. The Court erred in failing and refusing to make written findings of fact as required by law.

4. The Tax Court erred in finding:

> "Just when Schnack took down his share is not known * * *,"

the stipulation stating (Par. 4):

> "The payment of the $8,000 referred to therein was by check of the partnership drawn March 8, 1940."

5. The Court erred in finding:

> "Furthermore, due to the variance between the interests of Leffel and Ballentyne in the partnership it may not be said that the receipt by them on a 50-50 basis of the shares of the petitioner in exchange for the partnership assets represented a receipt by each of them of the said shares 'substantially in proportion to his interest in the property prior to the exchange' so as to

> make the exchange an exchange to which section 112(b)(5) was applicable,"

and in failing and refusing to find, as stated in the stipulation (Par. 4):

> "After the withdrawal of A. G. Schnack, Ballentyne and Leffel were equal partners in the business conducted by Hawaiian Freight Association."

6. The Court erred in finding (Tr. 52):

> "Except for Schnack's withdrawal of $8,000 * * * the record is silent as to withdrawals by any of the three partners."

the stipulation (Par. 10) showing an annual record of the capital, earnings and withdrawals of each partner and particularly showing that the balance of the profits of each year was withdrawn in the next year.

7. The Court erred in finding that the understanding between Leffel, Ballentyne and Oahu Railway and Land Company amounted to an "arrangement" or an "agreement", it being no more than a general understanding without legal force.

8. The Court erred in determining that "Schnack was not included in the plans for the new corporation", his nonparticipation being purely voluntary on his part.

9. The Court erred in finding:

> "Here there was no intention on the part of anyone that the partnership should continue,"

such finding being without evidentiary support and the stipulated facts clearly establishing that it did continue with Ballentyne and Leffel as equal partners from March 8, 1940 and until April 1, 1940, while petitioner was being organized and the transfers to it were being made.

10. The Court erred in failing and refusing to find that under the facts as stipulated and proved, and under the law of the Territory of Hawaii, the partnership, Hawaiian Freight Association was not terminated by Schnack's voluntary withdrawal, but continued for at least the brief period necessary to wind up its affairs, at least until April 1, 1940.

11. The Court erred in determining that the question of whether one partnership was terminated and a new partnership created by the withdrawal of Schnack could be answered without reference to the law of Hawaii, and in refusing to consider such law as applicable to the issue.

12. The Court erred in finding that petitioner did not acquire substantially all of the *assets* of Hawaiian Freight Association, and in failing and refusing to find that petitioner acquired substantially all of the *properties* of said predecessor partnership.

13. The Court erred in determining that the exchange by two equal partners (remaining after the withdrawal of Dr. Schnack) for petitioner's stock in equal amounts was not a tax-free exchange within the ambit of Section 112(b)(5).

14. The Court erred in failing and refusing to find and determine that the petitioner was entitled to the benefits of the optionally retroactive amendments to Supplement A provided by the Revenue Act of 1942.

15. The Court erred in failing and refusing to find and determine that the petitioner had made a valid election to have Supplement A as amended by the Revenue Act of 1942 applied retroactively.

16. The Court erred in failing and refusing to find and determine that the Commissioner was estopped to assert that a valid election for the retroactive application of Supplement A had not been made.

17. The Court erred in failing and refusing to find and determine that under the facts as stipulated and the evidence presented, the petitioner had made a *prima facie* case as to each and every issue involved in the proceeding, and that no contrary or contradictory evidence existed to refute such *prima facie* case.

18. If the Court did not err in determining that the partnership, Hawaiian Freight Association, was terminated by reason of Schnack's withdrawal, then the Court erred in failing and refusing to find and determine that the withdrawal of Schnack, the equalization of the interests of Leffel and Ballentyne, the organization of petitioner and the transfer of the partnership assets and business to petitioner were all parts of one transaction qualifying petitioner under Supplement A.

19. If the Court did not err in determining that the said partnership Hawaiian Freight Association was terminated on March 8, 1940, it erred in not determining that the respondent's regulation to the effect that a partnership cannot be an acquiring corporation was illegal and void as applied in this matter.

20. The Court erred in denying petitioner's motion for correction and enlargement of the Findings of Fact and Opinion, such denial being an abuse of discretion.

21. The Court erred in denying petitioner's motion for reconsideration, such denial being an abuse of discretion.

22. The Court erred in determining any deficiency against the petitioner for excess profits taxes for the years ended in 1943 and 1944.

SUMMARY OF ARGUMENT.

In the general scheme of excess profits taxes the basic Congressional purpose was to tax only abnormal profits due to the war. This usually was by reference to the taxpayer's earnings during the "normal period" 1936-1939. Relief was extended to corporations acquiring, tax free, the business and properties of predecessor organizations; the normal earnings of such acquired businesses could be used in determining what were not excess profits to the acquiring corporation.

On purely technical grounds of a minor change in membership of petitioner's predecessor partnership, immediately before petitioner's acquisition of its properties and business, respondent contended that this broad relief granted by Congress was not available to petitioner. Petitioner submits it is within the letter as well as within the spirit of the remedial legislation.

The Court below made no proper findings of the pertinent facts in controversy. In its opinion it distorted the facts as stipulated and as they appeared in uncontroverted documentary evidence. It assumed facts not in evidence but contrary thereto.

Certain issues were presented to the Court for its determination. The Court decided the controversy on issues never involved. Contrary to statute the controversy was decided, without excuse or reason, by a Division other than that to which presented.

In substance, the case as decided was on "facts" not presented, on "issues" not presented, and by a Division lacking jurisdiction. The ultimate determination on the merits was erroneous, petitioner being clearly entitled to the relief sought. A decision more clearly requiring reversal is difficult to imagine.

I. CONGRESS INTENDED, BY THE ENACTMENT OF "SUPPLEMENT A", TO ALLOW A CORPORATION IN PETITIONER'S POSITION TO USE THE EARNINGS EXPERIENCE OF ITS PREDECESSOR PARTNERSHIP.

The history and purpose of Supplement A demonstrate clearly its broad remedial purpose and that it was intended to benefit corporations such as petitioner.

The second revenue act of 1940 introduced an excess profits tax. The tax was levied on "adjusted excess profits net income", which was defined as "excess profits net income" minus the "excess profits credit" (with other adjustments not here material) (*I.R.C.* Sec. 710). The purpose of the "excess profits credit" was basically to allow a corporation its "normal" income free of excess profits tax. The determination of the excess profits credit could be made in either of two ways: (1) on the basis of its earnings during the base period, or (2) on the basis of a certain percentage of its invested capital. A corporation which was not in existence during the base period, having no base period earnings record, could determine its credit only by the invested capital method.

Some corporations, while technically not in existence during part or all of the base period, were essentially extensions of corporations which were in existence during the base period and were clearly equitably entitled to use the earnings experience of their predecessor; the business unit remained essentially the same. (If a business was carried on by a Nevada corporation during the base period and the state of

incorporation was changed to California at the beginning of the excess profits tax period—no other changes being made—the base period earnings of the Nevada corporation would certainly be a proper measure of the California corporation's "normal" earnings.) Supplement A (I.R.C. Secs. 740-744) therefore allowed certain corporations, which resulted from other corporations through certain tax free exchange, to use as their base period earnings experience the base period earnings experience of their predecessor corporation.

However, Supplement A as introduced in 1940, contained an obvious discrimination: It applied only where the taxpayer corporation acquired properties from a predecessor *corporation* (not a predecessor partnership or sole proprietorship). Obviously a business that was in existence during the base period in partnership form and was later incorporated could have a definite base period earnings experience by reference to which the "abnormal" profits of the successor corporation could be measured. Therefore, in 1941, *I.R.C.* Sec. 740(a)(1)(D) was enacted to include within the definition of an acquiring corporation (a corporation entitled to use the earnings experience of a predecessor, called a "component corporation") a corporation which grew out of a partnership or sole proprietorship.

The spirit in which *I.R.C.* Sec. 740(a)(1)(D) was enacted is demonstrated by the accompanying report of the House Ways and Means Committee (1941-1 *C.B.* pp. 550, 551, 552):

"In view of these compelling motives, the provisions of that Act lay a tax upon that portion of the earnings of corporations determined to be excess profits. The tax rates provided, or even higher rates, are thoroughly justified if the income subject thereto is clearly of the type intended to be reached. At the same time equitable considerations demand that every reasonable precaution be taken to prevent unfair application of the tax in abnormal cases. *The weight of the burden imposed carries with it a commensurate need for restricting its application to the cases for which it was designed."*

* * * * * * *

"For these reasons, the present legislation attempts to provide, both by specific terms and in carefully guarded general terms, a set of flexible rules which should alleviate at least the bulk of the severe hardship cases which may arise. *The success or failure of legislation of this type depends, to a considerable degree, upon its intelligent and sympathetic administration.* Through its confidence in the experience and ability of the officials of the Treasury Department and the Bureau of Internal Revenue, your committee recommend the present flexible and broad legislation as the most satisfactory method of meeting the contingencies that will arise.

So that the relief afforded by the bill may be available for the entire period covered by the excess profits tax, the provisions of this legislation are made retroactive to apply to taxable years beginning after December 31, 1939.

The bill affords relief in the following situations:

* * * * * * *

6. Under Supplement A of existing law, corporations resulting from certain tax-free exchanges or reorganizations during or after the base period are permitted the use of their predecessor's earning experience in the computation of their excess profits credit based on income. The bill extends this privilege to corporations growing out of partnerships or sole proprietorships in tax-free exchanges during this same period. The resulting corporation would thus be allowed to use the earnings history of the predecessor partnership or sole proprietorship, after first converting such earnings to a corporate basis." (Emphasis added.)

Thus Congress enacted *I.R.C.* Sec. 740(a)(1)(D) as a relief provision, designed to insure that only abnormal profits (those of the type intended to be reached by an excess profits tax) be taxed at excess profits tax rates. The relief provisions were necessarily drafted in carefully guarded terms and depended for their success on intelligent and sympathetic administration.

If Ballentyne and Leffel (the two active and continuing partners in Hawaiian Freight Association) had not, shortly before the incorporation of petitioner, bought out the interest of Schnack (the inactive, or investor, partner who held less than a 15% interest), there could be no doubt that petitioner is entitled to use the earnings experience of Hawaiian Freight Association. The Tax Court has held that petitioner is deprived of that right for a reason not well expressed but apparently because the inactive, minor "investor" partner was a member of the part-

nership for most but not all of its life, and was not a shareholder in petitioner corporation; the Tax Court did not deny, as it could not deny, that petitioner, upon its incorporation, was the same business unit, with the same operating assets and income potential, as Hawaiian Freight Association.

We submit that any decision denying petitioner the benefits of the earnings experience of the partnership which was so clearly the same business unit as petitioner, completely ignores the intent of Congress as well as the nature and function of Supplement A. It does not give the 1941 extension of Supplement A the "intelligent and sympathetic administration" Congress intended such provision to receive.

II. PETITIONER COMES SQUARELY WITHIN THE STATUTORY DEFINITION OF AN ACQUIRING CORPORATION.

Petitioner was within the letter, as well as the spirit, of the definition of an acquiring corporation.

I. R. C. Sec. 740, in material part provides:

> "Sec. 740. Definitions.
>
> For the purposes of this Supplement—
>
> (*a*) *Acquiring Corporation.*—The term "acquiring corporation" means—
>
> (1) A corporation which has acquired—
>
> * * * * * * *
>
> (D) Substantially all the properties of a partnership in an exchange to which section 112(b) (5), or so much of section 112(c) or (e) as refers

> to section 112(b)(5), or to which a corresponding provision of a prior revenue law, is or was applicable."

There are thus three requirements:

1. The corporation must acquire substantially all of the properties.

2. It must acquire them from a partnership.

3. The exchange must be within *I.R.C.* Sec. 112 (b)(5) either alone or as modified by Sec. 112(c) or (e).

We will deal with the first requirement, then the third and then the second, altering the order in order to dispose at the outset of the two requirements which can most easily be analyzed.

A. Petitioner acquired "substantially all of the properties" of Hawaiian Freight Association.

Perhaps the argument on this issue is unnecessary in view of the Court's determination (Tr. 47) "the *petitioner* in exchange for its 6,000 shares of stock *received the going business of Hawaiian Freight Association and most, if not all, of its remaining assets.*" (Emphasis supplied.) If unnecessary, counsel for petitioner offer their apologies to this Court.

As is elsewhere discussed more fully in this brief, dispute on this issue between counsel for the parties was narrow and technical; they were agreed that petitioner acquired substantially all of the properties of the continuing business. The question was whether

those properties were acquired from a new partnership or from a continuing partnership.

The determination of the Court that "it may not be said that petitioner acquired substantially all of the assets of the Hawaiian Freight Association in exchange for its stock" is a compound, ambiguous, conclusion. Apparently, and despite the fact that the Court found it unnecessary to clearly determine whether the partnership terminated on Schnack's withdrawal (Tr. 49-50), it premised this conclusion, not on the *quantum* of assets, but on their source in a partnership or tenancy in common in which Dr. Schnack was not a member (Tr. 43-44; 47, 110). The absence of proper findings of fact has unquestionably added greatly to the burden of counsel herein and, more importantly, to the burden of this Court.

The following argument is not restricted to the Tax Court's determination, but is intended as a more complete presentation on the merits particularly on the possible question that a distribution of surplus cash earnings not used in or necessary for the operation of the business, would prevent petitioner's right to relief.

Throughout the existence of Hawaiian Freight Association the partners followed the practice of withdrawing only a portion of the profits in the year in which the profits were made, withdrawing the remainder of such profits in the following year (after the amount of profits had been determined or could

reasonably be estimated). (Stip. par. 10, Tr. 35, 36). The total capital of the partnership was $16,984.12. Due to the time lag in withdrawal of profits the total capital plus accumulated earnings temporarily left in the partnership was as follows (Tr. 35):

Jan. 1, 1938 $36,192.36 (includes $16,984.12 capital)
Jan. 1, 1939 31,122.82 (includes $16,984.12 capital)
Jan. 1, 1940 33,927.86 (includes $16,984.12 capital)

The amount of accumulated earnings which a partner could withdraw was, of course, limited only by the capital required for the partnership's business. Generally, as noted above, slightly in excess of $30,000 (total capital plus accumulated earnings) was on hand in the partnership at the close of each year.

On March 8, 1940, the partnership interest of Dr. Schnack, the inactive partner, was bought for $8,000, payment being made from partnership funds. The $8,000 payment to Schnack represented his capital as well as accumulated earnings. However, Ballentyne and Leffel, the continuing partners, left enough of their accumulated earnings in the partnership to make up for much more than Schnack's capital account. The partnership assets, exclusive of goodwill, which petitioner acquired exceeded by over $13,000 the total capital of the partnership including Schnack's capital (Tr. 34, 35).

Ballentyne and Leffel also withdraw some of their accumulated earnings, as had been the custom throughout the existence of the partnership. But they

left in the partnership enough accumulated earnings so that petitioner could and did acquire from the partnership all the capital it needed for its operations (Stip. pars. 5 and 12, Tr. 34, 37).

On the above facts it was clearly erroneous for the Tax Court to conclude that petitioner did not acquire "substantially all of the assets[4] of the Hawaiian Freight Association" (Tr. 53). The basis for this conclusion is not clearly stated in the opinion. Apparently the Tax Court's holding was based on the fact that the remaining partners bought out all of Dr. Schnack's 14.9% interest (Tr. 96-98). Possibly the Tax Court was concerned with the fact that the remaining partners bought out Schnack's capital account ($2,534.03) as well as his accumulated earnings. (The Court was not concerned about the withdrawal of accumulated earnings. Tr. 96.)

But the partnership had no specific assets or properties which were peculiarly "Schnack's capital account". Such capital account was only a measure of Schnack's equitable ownership of a *quantum* of assets or properties held by the partnership. (The same properties were still in the partnership after Schnack withdrew and were still used in the business; only cash and undistributed earnings were reduced.) If Ballentyne and Leffel had the day before Schnack was bought out withdrawn $8,000 of accumulated earnings and used that $8,000 to buy out Schnack,

[4]The statute used the word "properties", which word as described infra, probably has a far more restricted meaning.

the fact that "capital" was left intact would be even easier to see. The actual method of buying out Schnack's interest had the same economic effect.

Clearly the withdrawal of profits from the partnership does not affect petitioner's standing as an acquiring corporation. If *I.R.C.* Section 740(a)(1)(D) required that earnings not be withdrawn from a partnership (even though retention was not necessary for business purposes) there would probably be not a single acquiring corporation which would be qualified within its meaning.

The Congressional intent behind the phrase "substantially all of the properties of a partnership" is not spelled out in any of the accompanying committee reports, or, so far as petitioner has been able to ascertain, in any reported case. However, the history of the successive versions of *I.R.C.* Section 740(a) gives some indication of the purpose and meaning of such phrase.

When the excess profits tax was first enacted in 1940 the House version of *I.R.C.* Sec. 740(a)(1)(A) used the words "substantially all of the *assets* of another corporation". The Senate changed the word "assets" to "properties" and also added *I.R.C.* Sec. 740(a)(1)(B) and (C). Section 740(a)(1)(D) was added in 1941, again using the phrase "substantially all the *properties*".

Two inferences seem reasonable: (1) "properties" is not the same as "assets", and (2) the phrase "sub-

stantially all the properties of another corporation" was taken from *I.R.C.* Sec. 112(g) where the same phrase is used. (This inference is very reasonable in view of the frequent references in the Committee Reports to the fact that Supplement A applies to certain *tax-free exchanges*).

The deliberate change in terms by the Senate cannot be ignored. If there is any difference in meaning (the Senate thought so and we submit that there is) the clearest example would be in the case of undivided profits held as surplus cash to the extent not used or required for the business. The cash would clearly be an asset, but not a portion of the "properties" of the business. The "properties" would be those assets which were used (including cash and accounts receivable) in the business to produce the undivided profits and surplus cash. Even if the transferor retained excess cash and earnings, the transfer would be of "substantially all the properties".

> *Commissioner v. First National Bank of Altoona* (C.C.A. 3, 1939), 104 F. (2d) 865, 870, 23 A.F.T.R. 119 (dismissed, 309 U.S. 691);
>
> *Western Industries Co. v. Helvering* (C.A.D.C., 1936), 82 F. (2d) 461, 17 A.F.T.R. 656;

c.f.:

> *Pillar Rock Packing Co., v. Com'r.* (C.C.A. 9, 1937), 90 F. (2d) 949, 19 A.F.T.R. 973.

In order to apply the case law on "substantially all the properties" in 112(g) to petitioner, the facts of this case must be analyzed as though Hawaiian

Freight Association were a corporation. On such analogy the facts would be these:

The "corporation" had a capital of $16,984.12. It distributed part of its earnings in the year in which such earnings were made, and the other part of its earnings in the following year. In 1940 cash dividends were declared and the stock of a minority shareholder was redeemed, all with surplus cash earnings. This left the corporation a total of $30,000 of assets, which assets included all of the corporation's operating properties plus enough cash to take care of its operating capital requirements. Such $30,000 of assets were then acquired by another corporation.

It has been decided that under the above stated facts the second corporation would have acquired "substantially all the properties" from the first corporation, even though the first corporation itself *retained* the surplus assets not used in the business.

> *Commissioner v. First National Bank of Altoona, supra.*

See also (to like effect):

> *John A. Nelson Co. v. Helvering* (1935), 296 U.S. 374, 56 S. Ct. 273;
>
> *G. & K. Mfg. Co. v. Helvering* (1935), 296 U.S. 389, 56 S. Ct. 276.

In view of the above case-defined meaning of the phrase "substantially all the properties of another corporation" it is clear that the phrase "substantially all the properties of a partnership" was intended to include the transfer made by Hawaiian Freight Asso-

ciation to petitioner. Petitioner acquired from Hawaiian Freight Association all of its operating properties, including accounts receivable, as well as its business and goodwill. Petitioner acquired a quantum of assets as great as that normally retained in the partnership. Petitioner acquired from Hawaiian Freight Association all the capital it needed for its operations. Petitioner therefore acquired "substantially all the properties" of Hawaiian Freight Association.

B. I.R.C. Section 112(b)(5) applied to the exchange by which petitioner acquired the properties of Hawaiian Freight Association.

Immediately prior to the formation of petitioner and the transfer of Hawaiian Freight Association's properties to petitioner, Ballentyne and Leffel were the sole and equal partners in Hawaiian Freight Association (Stip. par. 4, Tr. 33). Upon the incorporation of petitioner, Ballentyne and Leffel each owned fifty percent of petitioner's stock (Stip. par. 5, Tr. 33, 34). A clearer case of the applicability of *I.R.C.* Sec. 112(b)(5) would be hard to find. The Tax Court completely ignored the stipulated fact that Ballentyne and Leffel were equal partners after Schnack's withdrawal when it said:

> "Furthermore, due to the variance between the interests of Leffel and Ballentyne in the partnership it may not be said that the receipt by them on a 50-50 basis of the shares of the petitioner in exchange for the partnership assets represented a receipt by each of them of the said shares 'substantially in proportion to his interest in the

> property prior to the exchange' so as to make the exchange an exchange to which section 112(b)(5) was applicable." (Tr. 53.)

C. Despite the withdrawal of Dr. Schnack petitioner is entitled to use the earnings experience of Hawaiian Freight Association.

The primary dispute in the Tax Court concerned the issue of whether the Hawaiian Freight Association was one partnership or two successive and different partnerships. Respondent's contention was essentially as follows:

> When Dr. Schnack withdrew from Hawaiian Freight Association the partnership was dissolved and a new partnership was formed. Petitioner acquired the properties of the new partnership. By respondent's regulation a partnership cannot be an acquiring corporation. Since petitioner's only "component corporation" was, on this theory a partnership formed on March 8, 1940, petitioner was not constructively in existence on January 1, 1940 and therefore can not have an excess profits credit based on income.

In order to sustain this argument both of the following conclusions are necessary:

1. Schnack's withdrawal dissolved and terminated the partnership and resulted in a new partnership for the period required to form petitioner and complete the business in progress (22 days).

2. This technical change is sufficient to deprive the petitioner of the right to use the earnings experience of the partnership before dissolution.[5]

We shall now show that although respondent must win on both points to sustain his argument, he in fact can win on neither. The Tax Court did not clearly pass on this issue but held (1) contrary to the documentary fact, there was no intent to continue the partnership, and (2) there was no necessity to inquire into the continuity under Hawaiian law.

(1) Schnack's withdrawal did not dissolve the partnership and did not create a new partnership.

In determining whether Schnack's withdrawal dissolved the partnership we look first to the law of the territory under which the partnership was formed—the law of Hawaii. Compare *Cameron v. Commissioner,* 56 F. (2d) 1021 (C.C.A. 3, 1932) with *Carroll v. Commissioner,* 70 F. (2d) 806 (C.C.A. 5, 1934). The relevant Hawaiian statutes are set forth in Appendix A hereto.

The first point to be noted is that Hawaii in many respects accepts a partnership as an entity. It may be sued by firm name (Sec. 4048). Real and personal property taxes and a gross income tax are levied against partnerships in the firm name (Chapts. 61, 63 and 67).

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[5]The retirement of Dr. Schnack, of course, had no effect on the basis of the partnership properties or the basis of the remaining partners' interests in the partnership. It did not result in gain or loss either to the partnership or to the continuing partners.

The second point is that the Hawaiian statutes clearly imply that a general partnership is *not ipso facto* dissolved by the withdrawal of a partner. In particular Sec. 6862 provides in part:

> "*Statements of changes or dissolution.* Whenever any change shall take place in the constitution of any firm *by the death or withdrawal of any member thereof,* or by the addition of any member thereto, *or by the dissolution thereof,* * * *." (Emphasis added).

This accords with the modern view that:

> "By the general rule of law, death or withdrawal of a partner dissolves the partnership, *but it is competent for the parties to provide otherwise.*" (Emphasis added). *Robert E. Ford* (1946), 6 T.C. 499, 501. Acquiesced 1946-2 C.B.2.

The parties to the agreement whereby Schnack withdrew did provide that the partnership be not dissolved but continued. The agreement referred to Ballentyne and Leffel as "the remaining partners in the said co-partnership" (Tr. 39).

The closest case in point under the law of the Territory of Hawaii is *Lucas v. Lucas* (1911), 20 Hawaii, 433. In that case three brothers formed a partnership, one assigned his interest in the firm to a third party, and the third party was admitted by the other partners into the partnership. The Court quoted with approval, *Parsons on Partnership,* 4th Ed., Sec. 106:

> "One who represents the interest of a former partner, if received by the other partners and

> treated as a partner, becomes a partner under the original articles."

Being a partner in the original partnership, the new member could obtain an accounting of profits earned prior to the assignment to her and her admission.

As stated in *Lindley on Partnerships,* 10th Ed., p. 681:

> "Subject to a qualification which will be presently mentioned, a member of an ordinary firm can surrender his share and interest in the firm to his co-partners, or any of them, upon any terms to which he and they may all agree. But there is only one method by which a partner can retire from a firm without the consent of his co-partners, and that is, by dissolving the firm. In order to avoid the necessity of a general dissolution when a partner may wish to retire, special provisions are frequently introduced into partnership articles; but it is not infrequently found that, owing to unforeseen circumstances, these provisions cannot be carried into effect; and when that is the case, a dissolution, with its usual consequences, must take place if a partner is to retire otherwise than by the consent of his co-partner(s)."
>
> See, also, pages 499-501; 679-680; 682-683.

The third point is that even independent of the intention of the parties not to dissolve, Hawaiian law prevented dissolution until the filing of a certificate (Sections 6862 and 6863), which certificate was not filed for the Hawaiian Freight Association partner-

ship until after petitioner was incorporated and had acquired the properties of its predecessor partnership (Exhibits 4 and 5, Tr. 122-125; Stipulation par. 5, Tr. 33, 34).

Under Hawaiian law Hawaiian Freight Association was therefore one partnership from its formation until after the completion of the transfer of its business and properties to petitioner.

Even in jurisdictions where by statute the withdrawal of a general partner dissolves a partnership (there being no such statute in Hawaii) a judicial exception may be made where the withdrawing partner is a minor and inactive partner (as was Dr. Schnack). For example, in California (the jurisdiction whose case law most strongly influences Hawaii), even after the adoption of the Uniform Partnership Act the State Supreme Court has held that the death of a minor (20% interest) inactive partner did not dissolve a partnership. *Zeibak v. Nasser* (1938), 12 Cal. (2d) 1, at 17, 18, 82 Pac. (2d) 375 at 383.

Federal tax cases also lead to the conclusion that there was no dissolution of Hawaiian Freight Association when Dr. Schnack withdrew. The absence of dissolution under state law may be conclusive. *Cameron v. Commissioner, supra.* Furthermore, there is a decided trend in federal tax cases toward the recognition of a partnership as a separate entity for tax purposes. If a partnership is recognized as a separate entity for tax purposes clearly the entity is preserved when the continuing partners express the in-

tention to preserve it by continuing the partnership (as did the continuing partners in Hawaiian Freight Association), and the partnership is not dissolved.

One manifestation of the trend toward the entity theory in partnership tax law has been the series of cases holding that the death of a partner does not end the fiscal year of the partnership when the surviving partners continue the business.

> *Commissioner v. Mnookin Estate* (C.A. 8, 1950), 184 F. (2d) 89;
> *Girard Trust Company v. United States* (C.A. 3, 1950), 182 F. (2d) 921;
> *Henderson's Estate v. Commissioner* (C.C.A. 5, 1946), 155 F. (2d) 310.

Probably the best known result of the trend is the Commissioner's belated concession in *G.C.M.* 26379, 1950-1 C.B. 58 that the sale of a partnership interest is the sale of a capital asset. The Commissioner's concession came after he had lost numerous cases in which he argued that the sale of a partnership interest was not the sale of a capital asset because a partnership was not an entity separate and apart from its members (see, for example, *Daniel Gartling Estate* (1947), 6 T.C.M. 879, affirmed per curiam *Commissioner v. Estate of Gartling* (C.A. 9, 1948), 170 F. (2d) 73).

Even the last judicial stronghold of the "aggregate theory" (as opposed to the "entity theory") of the partnership in tax law—the United States Court of Appeals for the Second Circuit—has finally admitted

that, at least in some circumstances, the "entity theory" should be applied.

Goldberg's Estate v. Commissioner (C.A. 2, 1951), 189 F. (2d) 634.

The Court's recognition of the entity theory was expressed in a manner peculiarly appropriate to our case, when the Court said:

> "Unlike a corporation, which for tax purposes is treated as an independent jural personality, the partnership has been recognized by Congress as both a business unit and as an association of individuals. In determining the applicability of a specific tax code section to transactions involving partnerships decision must be governed not by reference to general *a priori* formulas drawn from the common law nature of a partnership, but by reference to the Congressional purpose for which the particular section was enacted." 189 F. (2d) at 635, 636.

In viewing the Congressional purpose for which Section 740(a)(1)(D) was enacted it is clear that the entity theory of the partnership must be applied (see pp. 14-18 *supra*).

Even respondent's regulations recognize that the withdrawal of a partner which does not materially affect the operation of the partnership business or the basis of its assets may not dissolve, but merely "reorganize" a partnership. Section 29.113(a)(13)-2 of *Regulations 111* provides in part:

> "*Readjustment of partnership interests.*—When a partner retires from a partnership, or a part-

> nership is dissolved, the partner realizes a gain or loss measured by the difference between the price received for his interest and the sum of the adjusted cost or other basis to him of his interest in the partnership plus * * *.
>
> If a new partner is admitted to the partnership, *or an existing partnership is reorganized,* the facts as to such change or reorganization should be fully set forth in the next return of income, in order that the Commissioner may determine whether any gain has been realized or loss sustained by any partner."

Thus Hawaiian Freight Association was not dissolved by Schnack's withdrawal. It was one and the same partnership both before and after such withdrawal.

Even if the partnership was dissolved, it was not terminated and a new partnership created. There was no intent to create a new partnership, but to continue the old one (Ex. A-1, Tr. 37-39). No certificate of a new partnership was filed as would have been required by Hawaiian law if a new partnership had been formed. The intent was to continue the old firm until the two remaining and equal partners had organized petitioner and conveyed the partnership business and properties to it. This was in accordance with an understanding[6] previously reached (Stip. pars. 3, 4; Tr. 33).

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[6]There is a great deal of difference in the legal meaning of "an understanding" resting on mutual advantage, as used in the stipulation of facts (Tr. 33) and "an agreement" or "an arrangement" as used by the Tax Court (Tr. 43, 45).

A distinction exists between termination and dissolution. The winding up process with its disposition of the assets occupies the intervening time between the two events.

See,

7 *Uniform Laws Annotated (Partnerships)*, p. 165.[7]

For the foregoing reasons it is submitted that the withdrawal of Dr. Schnack neither dissolved nor terminated the partnership in which he had been a minority and inactive member.

(2) Even if Dr. Schnack's withdrawal did cause a technical change in the partnership, petitioner is entitled to the benefits of Supplement A.

If this Court holds that Schnack's withdrawal did not terminate the partnership the following analysis is unnecessary to petitioner's case. If, however, this Court holds that such withdrawal did terminate the partnership it then becomes necessary to determine whether such change was a sufficient disruption of the partnership business to deprive petitioner of the earnings experience of the partnership prior to Schnack's withdrawal. We submit that Hawaiian Freight Association was so clearly one continuing business entity both before and after Schnack's withdrawal that petitioner is in any event entitled to use the total earnings experience of that one business

[7]The Commissioner's note clearly establishes that under all interpretations of common law there was a continuity of the partnership during the winding up period, at least for the purpose of suing and being sued.

entity from its organization on January 2, 1937, to its acquisition by petitioner in March, 1940.

In the first place, a technical dissolution of a partnership is now recognized as relatively ineffectual to bring about substantial changes in the tax treatment of a partnership. A technical dissolution by death or withdrawal will not (if the surviving partners continue the business as they did here) affect the partnership fiscal year as to the remaining partners (*Mary D. Walsh* (1946), 7 T. C. 205) or as to the deceased partner (*Comm'r v. Mnookin Estate* (C.A. 8, 1950), 184 F. (2d) 89); it will not affect the basis of the partnership assets (*Robert E. Ford* (1946), 6 T. C. 499); and it will not affect the holding period of a partnership interest (*Allan S. Lehman* (1946), 7 T.C. 1088, affirmed (C.A. 2, 1948), 165 Fed. (2d) 383). It should, therefore, not affect the right of a corporation to use the earnings experience of a predecessor partnership.

In the second place the history of the enactment of *I.R.C.* Sec. 740(a)(1)(D) (the section under which petitioner claims to qualify as an "acquiring corporation") demonstrates that its remedial intent extended to such a situation as herein presented, regardless of a technical and transitory change. As the Committee Reports to the enactment of *I.R.C.* Sec. 740(a)(1)(D) state:

> "Under Supplement A of existing law, corporations resulting from certain tax-free exchanges or reorganizations during or after the base period are permitted the use of the predecessor's

earning experience in the computation of their excess profits credit based on income. *The bill extends this privilege to corporations growing out of partnerships* or sole proprietorships *in tax-free exchanges* during this same period." (Emphasis added). (*Report of Committee on Ways and Means to Excess Profits Tax Amendments of 1941,* 1941-1 C.B. 550 at 552.)

As Mr. Cooper, in discussion from the floor of the House of Representatives, stated:

> "In other words, this provision makes it possible for a corporation in the taxable year to secure the advantage of the experience that its predecessor in business may have had, even though that predecessor was not a corporation as is provided for in existing law, but was a partnership." Vol. 87, *Congressional Record,* page 1380.

As the Tax Court stated in *Ransohoff's Inc.* (1947), 9 T.C. 376 at page 382:

> "There is no doubt that the petitioner corporation acquired and succeeded to the business organization of the Ransohoff partnership. We have held that the preceding partnership had a continuous existence. *The history of the earnings of that partnership, whether composed of Robert, James, and Howard, or of Robert and James, is a proper measure of the average base period net income of the petitioner for excess profits tax purposes.*" (Emphasis added).

The fact that the withdrawing partner was a minor inactive partner is important, not only as affects the

question as to whether there was a technical dissolution, but also as affects the materiality of a technical dissolution for the purposes of Supplement A. When an active partner *whose personal activities* are important to a partnership business, withdraws from a partnership a different business unit is in fact and substance created. If Ballentyne or Leffel (the two active partners) had withdrawn from Hawaiian Freight Association prior to the formation of petitioner a serious question might arise as to whether there was sufficient "continuity of business enterprise" to allow a successor corporation the earnings experience of the partnership prior to withdrawal. However, when the withdrawing partner is inactive and when his capital is retained in the business (by the continuing partners leaving in the business sufficient accumulated earnings) there is complete continuity of business entity.

The importance of continuity of business entity has been recognized, although not articulated, in prior Supplement A cases of predecessor partnerships or sole proprietorships. Where the asserted "component corporation" was the same business unit, taxpayers have been allowed the benefits of Supplement A.

> *Faigle Tool & Die Corp.* (1946), 7 T.C. 236;
>
> *A. C. Burton & Co. v. C.I.R.* (C.A. 5, 1951), 190 F. (2d) 115;
>
> *Ransohoff's, Inc.* (1947), 9 T.C. 376 (a case where the continuity of business entity was less clear than in petitioner's case, but where

the Court was much influenced by the liberal and remedial intent of Supplement A).

Where, however, the managing active partner has withdrawn so as to create a different business entity the taxpayer was not allowed the benefit of Supplement A.

E. T. Renfro Drug Co. v. C.I.R. (C.A. 5, 1950), 183 F. (2d) 846.

The very idea that a corporation is deprived of its predecessor partnership's earnings experience solely because there was a minor change in partnership personnel is so far from the spirit of "Supplement A" that the proposition seems to have been considered not even worth mentioning except in a very few instances. For example, in *Vegetable Farms, Inc. v. C.I.R.*, 191 F. (2d) ...., decided by this Court on Sept. 4, 1951, A, B, C, and D were partners in the vegetable growing business during the base period. On October 31, 1940, A and B bought out C and D. On November 8, 1940, A and B incorporated the business. The situation was identical with petitioner's situation[8] and neither the examining agent nor the government counsel in either stage of the litigation nor the Tax Court Judge nor any of the Judges of this Court questioned the taxpayer's right to the earnings experience of the four-man predecessor part-

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[8]Petitioner's right to the benefit of Supplement A is even stronger for in the *Vegetable Farms* case two partners withdrew (only one withdrew in petitioner's case) and in the *Vegetable Farms* case the withdrawing partners had rendered advisory services (while Dr. Schnack rendered none).

nership (the only argument being as to the amount of the Supplement A credit). We submit that petitioner's right to the benefit of Supplement A is similarly not open to questions.

III. PETITIONER IS ENTITLED TO THE RETROACTIVE APPLICATION OF SUPPLEMENT A TO TAXABLE YEARS BEGINNING BEFORE 1942.

This issue is subsidiary to the main issue discussed above. It affects the years in issue only in that it affects the amount of excess profits credit carry-over for years prior to petitioner's fiscal year ending on November 30, 1943.

Prior to the enactment of the Revenue Act of 1942 petitioner was not entitled to the benefits of Supplement A because the petitioner's "component corporation" (Hawaiian Freight Association, the partnership) was not in existence on January 1, 1936,[9] the beginning of petitioner's base period. Section 228 of the *Revenue Act of 1942* eliminated this requirement.

Section 228(f) of the *Revenue Act of 1942* provided that certain amendments made by Section 228 (including the amendments relevant to this issue) should apply to taxable years beginning before December 31,

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[9]Confusion as to the date of commencement of petitioner's base period and the existence of a component on that date is understandable in view of statutory changes and the complexity of the statutory language. Petitioner clearly believed that it did have a "qualified component" in existence on January 1, 1936 and could determine its excess profits credit on the earnings method.

1941, only if the taxpayer elected to have such amendments apply to such years. Petitioner submits that it complied with the spirit if not the letter of regulations relating to such election, and also that any failure of petitioner to comply with the letter of such regulations was induced by the conduct of respondent's agents.

The relevant statutes and regulations are set forth in Appendix B hereto. Section 30.742-2(e) of Regulations 109 required the electing taxpayer to file certain data, particularly:

(1) A statement that it elects to have such amendments apply retroactively;

(2) Certain data and computatioss for each of such years.[10]

Petitioner at all times believed that it was entitled to the benefits of Supplement A, even without the 1942 amendments. It filed all its excess profits tax returns (including a return before the 1942 act was passed) on the assumption that it was entitled to the earnings experience of its predecessor partnership. All of its returns contained the necessary data and information required by the regulations. All its returns indicated a clear intent to avail itself of Supplement A. The Commissioner now states, however, that petitioner is not entitled to the retroactive application of Supplement A for the taxable years begin-

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[10]The data and computations required were the same as set forth on the several excess profits tax returns filed by petitioner for the respective years.

ning before 1942 because petitioner, believing the 1942 amendment not necessary to give it Supplement A benefits, did not perform the ritual of attaching a statement to its return announcing a formal election to have Supplement A apply retroactively.

Petitioner's conduct did not mislead the Commissioner in any way. Petitioner supplied the Commissioner with all relevant schedules and data for the computation of the Supplement A credit. Petitioner used Supplement A for taxable years beginning before 1942 in excess profits tax returns filed both before and after the enactment of the Revenue Act of 1942. Petitioner, after the Revenue Act of 1942, submitted in its Tax Court petition that it was entitled to the benefit of Supplement A for the fiscal years beginning in 1940 and 1941 (6 *T.C.M.* 601). Its disclosure was complete; its conduct bona fide. Its intention to use Supplement A retroactively was and is, we submit, clear to anyone with any understanding of the Internal Revenue Code (and certainly clear to the Commissioner).

Unfortunately the petitioner was not informed of the Commissioner's intention as clearly as the Commissioner was informed of the petitioner's intention. At a time when petitioner could probably still have filed in time the requisite formal statement of election[11] the Commissioner led petitioner to believe that

[11]The probable interpretation of Sec. 30.742-2(e) of Regulations 109 as set forth in *T.D. 5242, 1943 C.B. 692* at *734* is that petitioner originally had until February 15, 1944 to file such statement. The

no such statement was necessary, by approving petitioner's use of Supplement A for fiscal years beginning in 1940 and 1941. Only when it was too late for petitioner to file a formal statement of election did the Commissioner (who with fine impartiality now champions form over substance) decide that the formal election statement is necessary.

We submit that since the Commissioner at all relevant times was supplied with all necessary information and abundantly clear evidence of intention to have Supplement A apply retroactively, petitioner is entitled to the retroactive application of Supplement A.

IV. NUMEROUS ERRORS BY THE TAX COURT REQUIRE ITS REVERSAL.

The errors committed by the Tax Court, other than the ultimate determination against petitioner, fall into four main classes:

A. The Court failed to make findings of fact as required by law;

B. The Court made factual statements contrary to the stipulated facts;

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clear inference from *T.D. 5391* as amended by *T.D. 5400 (1944 C.B. 474, 476)* is that the time for making the election provided by *Section 30.472-2(c)* of Regulations 109 was extended for a reasonable period after August 22, 1944 (the date of promulgation of *T.D. 5400*). However the Revenue Agent, under Report dated June 2, 1944 (Pet. Exs. 7 and 8, Tr. 126, 127) approved petitioner's use of Supplement A for 1941 and 1942 giving petitioner no clue that an additional statement had to be filed.

C. The Court's determination was essentially on "issues" not before it, and apparently predicated upon assumed "facts" not in evidence but contrary thereto;

D. The Court exceeded its jurisdiction in that the findings of fact and opinion were made by a Division different from that hearing the controversy.

These errors unquestionably had a cumulative effect on the ultimate determination of the Court, an effect more important than if the errors had all been of a single class.

A. The Court failed to make findings of fact as required by law.

The Tax Court is required to make written findings of fact. This is one, if not the most important, principal function of the Court.

> *I.R.C.* Sec. 1117(b);
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> *Diller v. Commissioner* (C.A. 9, 1936), 91 F. (2d) 194;
>
> *Belridge Oil Co. v. Helvering* (C.A. 9, 1934), 69 F. (2d) 432;
>
> *Levitt & Sons, Inc. v. Nunan* (C.A. 2, 1944), 142 F. (2d) 795.

The case was presented to the Court, in part on a written stipulation of facts, but in part upon documentary exhibits and an oral stipulation. Respective counsel on brief presented proposed findings of fact, predicated in part on the stipulations and in part on the documentary exhibits.

The Court stated (Tr. 44):

> "The facts have been stipulated and as stipulated are so found."

This was the only finding made by the Court with respect to the evidence before it (Tr. 87). It was very careful not to make findings in its opinion (Tr. 87-88).

Counsel for the respective parties were in agreement as to the evidentiary facts; these were stipulated or admitted without objection. Counsel did not agree as to the following ultimate facts:

(1) Whether the partnership was terminated by Schnack's withdrawal;

(2) Whether a new partnership was then formed;

(3) Whether petitioner had made an effective election or whether the respondent was estopped to otherwise contend;

(4) Whether petitioner was an acquiring corporation.

These were the essential facts to be determined by the Court from the evidence submitted, documentary or stipulated. That is what the Court should have done in fulfillment of its essential function, and it is what the Court failed and refused to do.

B. The Court made factual statements contrary to the stipulated facts and other evidence.

Perhaps because the Court failed to make appropriate findings of fact, perhaps because it easily and

simply stated it found the facts as stipulated, perhaps for other reasons unknown to counsel, it in any event did make a number of factual misstatements. These were so material in nature that it cannot be assumed the same result would have been reached in the absence of such misstatements.

The parties stipulated that Schnack was paid on March 8, 1940 (Tr. 33, 39). The Court stated: "Just when Schnack took down his share is not known." (Tr. 50).

The agreement with Schnack referred to Leffel and Ballentyne as the remaining partners in the partnership and provided that future operations would be at their risk (Tr. 38-39). It was stipulated that thereafter Ballentyne and Leffel were equal partners in the business (Tr. 33). The Court stated: "Here there was no intention on the part of anyone that the partnership should continue." (Tr. 50).

The parties stipulated that an understanding had been reached for the formation of petitioner (Tr. 33). Without further evidence the Court made this "an arrangement and understanding" (Tr. 45, 46), "agreements and understandings" (Tr. 51) and in the official headnote (Tr. 43) it is called "an agreement."[12]

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[12]An agreement was subsequently reached on July 12, 1940. See *Hawaiian Freight Forwarders, Ltd. v. Com'r,* 6 T.C.M. 601, in which the same issue as here presented was involved but not decided, and which counsel and the judge to whom the case was presented were also identical.

The parties stipulated that "after the withdrawal of A. G. Schnack, *Ballentyne and Leffel were equal partners* in the business conducted by Hawaiian Freight Association". (Tr. 33). The Court stated (Tr. 53): "* * * *due to the variance between the interests of Leffel and Ballentyne*" their receipt of the stock of petitioner on a 50-50 basis was not substantially in proportion to their interests in the property prior to the exchange.

C. The Court's determination was essentially on "issues" not before it and apparently predicated upon assumed "facts" not in evidence but contrary thereto.

The Commissioner's determination is presumptively correct. The Commissioner determined that no gain or loss was recognized by the petitioner in the transfer of the properties of the predecessor partnership in exchange for its stock. Thus, in computing petitioner's excess profits credit on the invested capital basis, the original cost to the partnership (rather than fair market value at the time of transfer) was used as the cost of such stock (Tr. 16, 19). This was the amount transferred, exclusive of goodwill, which had cost the partnership nothing (Tr. 34).

The pleadings did not serve to fully define the issues in controversy, the respondent's answer being a general denial. The Commissioner having determined the transaction to be tax free, i.e., within the scope of Section 112(b)(5) of the Code no assignment of error appears with respect thereto in the petition. By the time the stipulation of facts was drawn, respective

counsel were agreed as to the points of controversy. This is reflected in the stipulation itself, particularly at paragraph 13 (Tr. 37):

> "That portion of the foregoing stipulation which deals with the earnings of the Hawaiian Freight Association for the three months ended March 31, 1940, shall not be regarded as a concession on the part of respondent that only one partnership was in existence during the said period, it being the respondent's position that the elimination of A. G. Schnack as a partner on March 8, 1940 terminated the existing partnership and resulted in the creation of a new partnership on that date."

In the hearing before the Court (Division 9) respective counsel made opening statements defining the issues presented to the Court for its determination. In them there was not the slightest suggestion as to an issue under Section 112(b)(5) of the Code. Under the written stipulation of facts and the Commissioner's determination Section 112(b)(5) was clearly applicable, so nothing was said about it.

Therefore the issues presented to and argued before the Court related to the continuity of the partnership from March 8 to April 1, the period required to wind up business in process, and the effect of such continuity on petitioner's right to relief. If this was not a new partnership, petitioner was clearly entitled to prevail; less clearly if it was a new partnership. As an ancillary issue, in reality a different approach to the same issue, respondent contended that petitioner

did not acquire substantially all of the properties of *the "old partnership"* but instead, those of a new partnership.

Unquestionably the assets acquired by petitioner had a value greater than cost to the predecessor partnership. This was particularly true of goodwill, as indicated by the earnings of the partnership. Because the facts clearly precluded any argument that the transfer was not within the scope of Section 112(b)(5), petitioner could not and did not urge that it was. Otherwise, petitioner could have had a higher excess profits credit on the invested capital basis, i.e., 8% of the increase in the value of the assets transferred over original cost to the predecessor partnership.

Thus petitioner is in the position of having a case decided against it on a basis not presented or argued and with no opportunity to effect the tax saving inherent in the predicates of the decision. The stipulation of facts and other evidence and the argument thereon were entirely adequate to meet the issues actually in controversy, but not to meet the "facts" and "issues" as assumed by the Tax Court.

The function of an opening statement is to advise the Court of the salient facts and of the issues presented for its decision. The admissions and concessions frequently made therein, either directly or by implication, greatly minimize the work of the Court; they are not meaningless.

9 *Mertens, Federal Income Taxation,* 269-271, and cases cited;

Com'r v. Lawrence Operating Company, 152 F. (2d) 938 (C.A. 2, 1945).

In part predicated upon failure to adhere to the stipulated facts and uncontroverted documentary exhibits, and in part predicated on distortion of such evidence the Court concluded (without clear and logical reasoning):

1. There was no intention on the part of anyone that the partnership should continue (Tr. 50);

2. It was therefore unnecessary to determine whether it did in fact or law continue (Tr. 49-51);

3. Petitioner did not acquire substantially all the assets of the partnership which commenced January 2, 1937 and which continued to the time "the agreements and understandings were reached" (Tr. 51, 53);

4. Due to the *variance* of the interests of Ballentyne and Leffel their receipt of the stock of petitioner on an equal basis was not in proportion to their interests in the partnership properties (Tr. 53).

As elsewhere discussed these conclusions are contrary to the agreed and incontrovertible facts and evidence. They do not answer the question: What was the effect of Schnack's withdrawal? i.e., (1) Was the partnership continued? (2) Was it dissolved and in the process of winding up; or (3) Was it terminated and a new partnership formed?

After the promulgation of the Tax Court's Findings of Fact and Opinion petitioner moved for the correction and enlargement of the Findings of Fact and also moved for reconsideration (Tr. 4). Both of such motions were denied (Tr. 5).

In substance what the Court did was not only to decide the controversy on issues not presented, but to fail to decide the essential issue which was presented. The case decided was never before it; the case before it was never decided.

D. The Court exceeded its jurisdiction in that the findings of fact and opinion were made by a division different from that hearing the controversy.

In addition to the substantive errors detailed above there was a procedural error in the trial of this case in the Tax Court: the case was heard by and argued before Judge Van Fossan (Division 9) and was then assigned to and decided by Judge Turner (Division 8) (Tr. 42). No reason was given for the transfer.

The Tax Court is a creature of statute. Its powers are defined in the statute. The statute provides:

> *I.R.C. Sec. 1103:*
>
> "(c) *Divisions.*—The chairman may from time to time divide the Board into divisions of one or more members, assign the members of the Board thereto, and in case of a division of more than one member, designate the chief thereof. * * *."
>
> *I.R.C. Sec. 1118:*
>
> "(a) *Hearings, Determinations and Reports.*—A division shall *hear, and make a determina-*

> *tion upon,* any proceeding instituted before the Board and any motion in connection therewith, assigned to such division by the chairman, and shall make a report of any such determination which constitutes its final disposition of the proceeding." (Emphasis added.)

Thus there is authorization to divide the Tax Court into divisions. There is provision for a division to hear a case (as was done here, the division being Judge Van Fossan). There is also statutory authorization for the division that hears the case to decide it (as is done every day in the Tax Court). But there is no authorization for one division (here Division Nine) to hear, and for another division (here Division Eight) to determine a case, as was done here. Such procedure is not authorized by statute and is not necessary to implement any power authorized by statute. Such procedure is therefore not within the power of the Tax Court—a Court of limited jurisdiction and power.

A judicial exception to the above statutory provisions has been made allowing one Tax Court judge to decide a case heard by another judge in exceptional circumstances, namely when the judge who heard the evidence died or resigned before decision or when the term of the judge who heard the evidence expired before decision. There have been five such cases:

Foss v. Commissioner (C.C.A. 1, 1935), 75 F. (2d) 326 (Death);

Garden City Feeder Co. v. Commissioner (C.C.A. 8, 1935), 75 F. (2d) 804 (Death);

Davidson v. Commissioner (C.C.A. 5, 1937), 91 F. (2d) 516 (Resignation);

Seaside Improvement Co. v. Commissioner (C.C.A. 2, 1939), 105 F. (2d) 990 (Resignation);

Halle v. Commissioner (C.A. 2, 1949), 175 F. (2d) 500 (Expiration of term of office).

For present purposes it is sufficient to note that the exceptional circumstances involved in each of the above cases was not present in this case (Judge Van Fossan who heard the case remained an active member of the Tax Court). There is, therefore, no basis in the case law or otherwise for the procedure followed by the Tax Court in this case in direct violation of statute.

Petitioner prefers a decision on the merits to one on this point. Petitioner raises this procedural point because it is clear that as a practical matter petitioner's rights were impaired by the transfer of this case, after hearing, from Judge Van Fossan to Judge Turner. Judge Van Fossan had heard a prior case between the same parties involving petitioner's right to the benefit of Supplement A.[13] He also heard this case. He was therefore familiar with the facts and issues which determine petitioner's right to Supplement A. It is therefore inconceivable that Judge Van Fossan could have decided this case on legal issues which counsel conceded were not involved, and on facts which were contrary to the stipulation.

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[13]In 6 *T.C.M.* 601. Petitioner's right to the benefit of Supplement A was presented as an alternative issue—an issue that was never decided because petitioner prevailed on the main issue.

V. CONCLUSION.

For the above reasons it is submitted that the decision of the Tax Court was clearly erroneous and should be reversed with directions to enter a decision of no deficiency.

Dated, San Francisco, California,
November 5, 1951.

Respectfully submitted,
LOUIS JANIN,
HAROLD E. HAVEN,
MELVIN H. MORGAN,
Counsel for Petitioner.

(Appendices A and B Follow.)

Appendices A and B.

Appendix A

HAWAIIAN LAWS.

All references are to Revised Laws of Hawaii 1935—the most recent bound edition published at the time Dr. Schnack withdrew from Hawaiian Freight Association (March 1940).[1]

Sec. 6862 [8604]

"Sec. 6862. *Statements of changes or dissolution.* Whenever any change shall take place in the constitution of any firm by the death or withdrawal of any member thereof, or by the addition of any member thereto, or by the dissolution thereof, a statement of the change or dissolution shall also be filed in the office of the treasurer, on blanks to be furnished by the treasurer, within thirty days from the change, death or dissolution, and acknowledged before a notary public in the manner provided by law for the acknowledgment of deeds, as the case may be."

Sec. 6863 [8606]

"Sec. 6863. *Statements to be published.* All such statements as are required to be made in the preceding sections, except those required to be filed annually, shall also be published by the members of each copartnership at least twice in the English language, in any newspaper of general circulation published in each county and city

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[1]Bracketed section numbers are references to corresponding section of Revised Laws of Hawaii 1945.

and county where the copartnership has a place for the transaction of business."

Sec. 6864 [8607]

"Sec. 6864. *Record of statements.* The treasurer shall cause a book to be kept in his office, in which shall be recorded the several particulars in this subtitle before required to be filed in his office; and the book shall be open for public inspection."

Sec. 6866 [8609]

"Sec. 6866. *Personal liability and penalty.* The members of every copartnership who shall neglect or fail to comply with the provisions of this subtitle shall severally and individually be liable for all the debts and liabilities of the copartnership, and may be severally sued therefor, without the necessity of joining the other members of the copartnership, in any action or suit, and shall also severally forfeit to the Territory twenty-five dollars for each and every month while the default shall continue, to be recovered by action brought in the name of the Territory by the treasurer." [as amended in 1937.]

Chapter 61, Administration and Real Property Tax.

Sec. 1925 [5142]

"Sec. 1925. *Assessment of property of corporations or co-partnerships.* Property of a corporation or co-partnership shall be assessed to it under its corporate or firm name."

Chapter 63, Business Excise Tax.

Sec. 2000[2]

"Sec. 2000. *Excise tax.* There shall be levied and assessed each year upon each person doing business within the Territory, except as otherwise in this chapter provided, an excise tax in the manner and at the rate hereinafter provided, for the doing of business for the taxable year preceding the one in which the tax is regularly assessed. Such tax shall be in addition to any license or other fee prescribed by any other law."

Sec. 2001[2]

"Sec. 2001. *Definitions.* Whenever used in this chapter . . .

'Person' shall include every individual, partnership . . ."

Chapter 67, Personal Property Tax.

Section 2107 [5637]

"Sec. 2107. *Assessment of property of corporations or copartnerships.* Property of a corporation or copartnership shall be assessed to it under its corporate or firm name."

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[2]No exactly corresponding section, but see sections 5442, 5455 of Revised Laws of Hawaii 1945.

Appendix B

FEDERAL TAX STATUTES AND REGULATIONS.

I.R.C. Sec. 112(b)(5)

"(5) Transfer to Corporation Controlled by Transferor. No gain or loss shall be recognized if property is transferred to a corporation by one or more persons solely in exchange for stock or securities in such corporation, and immediately after the exchange such person or persons are in control of the corporation; but in the case of an exchange by two or more persons this paragraph shall apply only if the amount of the stock and securities received by each is substantially in proportion to his interest in the property prior to the exchange. Where the transferee assumes a liability of a transferor, or where the property of a transferor is transferred subject to a liability, then for the purpose only of determining whether the amount of stock or securities received by each of the transferors is in the proportion required by this paragraph, the amount of such liability (if under subsection (k) it is not to be considered as 'other property or money') shall be considered as stock or securities received by such transferor."

I.R.C. Sec. 712. *Excess Profits Credit—Allowance.*

"(a) Domestic Corporations.—In the case of a domestic corporation which was in existence before January 1, 1940, the excess profits credit for any taxable year shall be an amount computed under section 713 or 714, whichever amount

results in the lesser tax under this subchapter for the taxable year for which the tax under this subchapter is being computed. In the case of all other domestic corporations the excess profits credit for any taxable year shall be an amount computed under section 714. For allowance of excess profits credit in case of certain reorganizations of corporations, see section 741."

I.R.C. Sec. 713. *Excess Profits Credit—Based on Income.*

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I.R.C. Sec. 714. *Excess Profits Credit—Based on Invested Capital.*

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I.R.C. Sec. 740. *Definitions.*

"For the purposes of this Supplement—

(a) Acquiring Corporation.—The term 'acquiring corporation' means—

(1) A corporation which has acquired—

(A) substantially all the properties of another corporation and the whole or a part of the consideration for the transfer of such properties is the transfer to such other corporation of all the stock of all classes (except qualifying shares) of the corporation which has acquired such properties, or

(B) substantially all the properties of another corporation and the sole consideration for the transfer of such properties is the transfer to such other corporation of voting stock of the corporation which has acquired such properties, or

(C) before October 1, 1940, properties of another corporation solely as paid-in surplus or a contribution to capital in respect of voting stock owned by such other corporation, or

(D) substantially all the properties of a partnership in an exchange to which section 112(b)(5), or so much of section 112(c) or (e) as refers to section 112(b)(5), or to which a corresponding provision of a prior revenue law, is or was applicable.

* * * * * * *

(b) Component Corporation.—The term 'component corporation' means—

(1) In the case of a transaction described in subsection (a)(1), the corporation which transferred the assets;

(2) In the case of a transaction described in subsection (a)(2), the corporation the property of which was acquired;

(3) In the case of a statutory merger, all corporations merged, except the corporation resulting from the merger; or

(4) In the case of a statutory consolidation, all corporations consolidated, except the corporation resulting from the consolidation; or

(5) In the case of a transaction specified in subsection (a)(1)(D), the partnership whose properties were acquired.

* * * * * * *

(d) In the case of a taxpayer which is an acquiring corporation the base period shall be the four calendar years 1936 to 1939, both inclusive,

except that, if the taxpayer became an acquiring corporation prior to September 1, 1940, the base period shall be the same as that applicable to its first taxable year ending in 1941.

(e) Base Period Years.—In the case of a taxpayer which is an acquiring corporation its base period years shall be the four successive twelve-month periods beginning on the same date as the beginning of its base period.

(f)[1] Existence of Acquiring Corporation.—For the purposes of subsection (c) and section 741, if any component corporation was in existence on the date of the beginning of the taxpayer's base period (either actually or by reason of this subsection), its acquiring corporation shall be considered to have been in existence on such date.

(f)[2] Existence of Acquiring Corporation.—For the purposes of Section 712(a), if any component corporation of the taxpayer was in existence before January 1, 1940, the taxpayer shall be considered to have been in existence before such date.

(g) Component Corporations of Component Corporations.—If a corporation is a component corporation of an acquiring corporation, under subsection (b) or under this subsection, it shall (except for the purposes of section 742(d)(1) and (2) and section 743(a)(1), and (3)) also be a component corporation of the corporation of which such acquiring corporation is a component corporation."

[1]Before amendment by Sec. 228 of the Revenue Act of 1942.
[2]After amendment by Sec. 228 of the Revenue Act of 1942.

I.R.C. Sec. 742. *Supplement A Average Base Period Net Income.*

"In the case of a taxpayer which is an acquiring corporation, its average base period net income (for the purpose of the credit computed under section 713) shall be the amount computed under section 713 or the amount of its Supplement A average base period net income, whichever is the greater.

* * * * * * *

(g) In the case of a partnership which is a component corporation by virtue of section 740(b) (5), the computations required by this Supplement shall be made, under rules and regulations prescribed by the Commissioner with the approval of the Secretary, as if such partnership had been a corporation. For the purpose of such computations, in making the adjustment for income taxes required by section 711(b)(1)(A), the partnership so regarded as a corporation shall be considered as having distributed all its net income as a dividend."

Revenue Act of 1942, Sec. 228:

"(f) Taxable Years to Which Amendments Applicable.—The amendments made by this section shall be applicable only to the computation of the tax for taxable years beginning after December 31, 1941, except that (1) the last sentence of section 740(c), as added by subsection (a) of this section shall be applicable to the computation of the tax for all taxable years beginning after December 31, 1939, and (2) if a taxpayer, within the time and in the manner and subject to such

regulations as the Commissioner with the approval of the Secretary prescribes, elects to have such amendments (except those which by their terms are limited to taxable years beginning after December 31, 1941, and except that referred to in clause (1)) apply retroactively to all taxable years of the taxpayer beginning after December 31, 1939, such amendments shall also be applicable to the computation of the tax for taxable years beginning after December 31, 1939."

Regulations 112, Sec. 35.740-4

"* * * a partnership (or a business owned by a sole proprietorship) cannot be an acquiring corporation. * * *"

Regulations 109, Sec. 30.742-2(e) as amended by T.D. 5242, 1943 C.B. 692 at 734:

"(e) *Election to have amendments to Supplement A made by Revenue Act of 1942 apply to taxable years beginning after December 31, 1939, and before January 1, 1942.*—A taxpayer may elect to have the amendments to Supplement A made by the Revenue Act of 1942 apply retroactively (with the exceptions indicated below) to all its taxable years beginning after December 31, 1939, and before January 1, 1942. If a taxpayer elects to have such amendments so apply, each such amendment shall be applicable to such taxable years, except such of the amendments as by their terms are limited to taxable years beginning after December 31, 1941. The election does not apply to the last sentence of section 740(c), as added by the Revenue Act of 1942, or to the repeal of section 741(b), which amend-

ments by their terms are retroactive to all taxable years beginning after December 31, 1939. The amendments which by their terms are limited to taxable years beginning after December 31, 1941, and therefore are also not subject to the election are the provisions of section 740(c) (except the last sentence thereof) and section 742(b)(2).

"If the taxpayer desires to make the election described in the preceding paragraph, the election must be made on or before whichever one of the following applicable dates occurs first:

(1) June 15, 1943, if an excess profits tax return for a taxable year beginning after December 31, 1941, is filed for such year, and if such return is filed on or before June 15, 1943,

(2) the date of the filing of the taxpayer's excess profits tax return for its first taxable year beginning after December 31, 1941, for which an excess profits tax return is filed if such return is filed after June 15, 1943, or

(3) the date of expiration of 30 months after the filing of the excess profits tax return (or, if no such return was filed, after the date on which such return was due or would have been due if such return were required to be filed) for the taxpayer's first taxble year beginning after December 31, 1939.

The election once made shall be irrevocable and shall apply to all taxable years of the taxpayer beginning before January 1, 1942.

In order to make such election, the taxpayer shall, within the time prescribed, file with the collector the following:

(i) A statement that the taxpayer elects to have such amendments apply to each of the taxable years beginning after December 31, 1939, and before January 1, 1942; and

(ii) A statement with respect to each such taxable year setting forth (A) the Supplement A average base period net income for such taxable year, computed under Supplement A as amended by such amendments, (B) the excess profits credit for such year based upon the Supplement A average base period net income for such year so computed, and (C) the excess profits tax or unused excess profits credit (as defined in section 710(c)(2)), if any, as the case may be, for such year resulting from the use of the excess profits credit so computed. Such statement shall not constitute a claim for credit or refund. If the application of the amendments made by the Revenue Act of 1942 results in an overpayment in the amount of tax for any taxable year, a timely claim for credit or refund on Form 843 should be filed in the usual manner. For limitations upon credits and refunds generally, see section 322."

T. D. 5391 as amended by T. D. 5400, 1944 C. B. 474, 476.

"Subpart IV—Miscellaneous Provisions.

Extension of time for making certain elections. —If in these regulations a time is fixed on or before which an election or application for relief may be made by the taxpayer and such time is not expressly provided in the law, the Commissioner in his discretion may, for good cause

shown, except as provided in the next paragraph, grant a reasonable extension of time for the making of such election or application if request for such extension is filed with the Commissioner prior to the time fixed for making such election or application or within such time thereafter as the Commissioner may consider reasonable under the circumstances and it is shown to the satisfaction of the Commissioner that the granting of the extension will not jeopardize the interests of the Government.

"The time fixed in these regulations will not be extended by the Commissioner in such cases as the following: (a) an election required to be made in or with the taxpayer's original income or excess profits tax return; (b) an election required to be exercised by the filing of a claim for credit or refund unless such election is required to be exercised at a time fixed by these regulations, which time is before the date of the expiration of the period of limitations provided in section 322, or an election required to be filed in a petition to the Tax Court; or (c) an application for permission to change a previous election.

Regulations * * * 109

"*Par. 4.* The above amendments to Regulations * * * 112, which regulations are applicable to taxable years beginning after December 31, 1941, are hereby made applicable to any taxable year beginning * * * after December 31, 1939, and prior to January 1, 1942, which is covered by Regulations 109. (T.D. 5391, July 14, 1944, as amended by T.D. 5400, Aug. 22, 1944.)"